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¶1. (U) Summary. This is Volume 8, issue 24 of U.S. Embassy Pretoria's South Africa Economic News Weekly Newsletter.

Topics of this week's newsletter are:
- World Bank Upbeat on SA Economy
- Another Interest Rate Hike
- Current Account Deficit Raises Concern
- Electricity Problems Likely to Harm Economic Growth Objectives
- Banks Tighten Discount Screws on Home Buyers
- Cash Is King as Rate Hikes Sting Shoppers
- World Economic Forum on Africa
- SA Air Force Pilots Jet-Off to Australia
- Delta Optimistic About Africa Expansion
- Airports on Track for 2010, But ACSA Concerned about High Borrowing Costs
- Guatrain on Track for 2010
- Motor Industry Running on Empty
- Mercedes-Benz SA Expands Truck Range
- Electricity Distribution Maintenance Backlog
- Another Electricity Crisis Looms
- Minister Says Suez Energy Submitted Binding Offer for IPP Project
- U.S. Gold Miner in SA
- Canadian Business Chamber Flays SA
- Unions Give Telkom Silent Treatment
- Dubai World Plans to Expand in SA
End Summary.

World Bank Upbeat on SA Economy

¶2. (U) The World Bank expects SA's economy to grow by a robust 4.2% this year, slightly above official estimates of 4.0% and surpassing consensus forecasts for a sharp slowdown prompted by higher interest rates, power shortages and global risk aversion. Consensus forecasts from a June Reuters poll predicted SA's pace of growth will slow to 3.4% this year from an average of 5% over each of the past four years. The World Bank 2008 Global Development Finance Report author Hans Timmer said rising investment in power plants and other infrastructure would help offset waning consumer demand and the bleaker global investment mood. He emphasized that "there is underlying growth potential in SA and it will continue". Timmer said household consumption, which accounts for about 60% of SA's economy, was slowing gradually while investment was rising rapidly. SA's main investment indicator surged to 20% of gross domestic

product (GDP) last year from 15% in 2000, spurred mainly by capital investment by state entities. The World Bank sees economic growth accelerating to 4.4% in 2009 and 4.8% in 2010, also above official forecasts. (Business Day, June 11, 2008)

Another Interest Rate Hike

¶3. (U) The SA Reserve Bank's (SARB's) monetary policy committee has raised its key lending rate, the "repo" rate by 50 basis points to 12%, taking the prime lending rate to 15.5%. The consensus forecast by 10 leading economists polled by I-Net Bridge was for a 100-basis-point increase in the repo rate. The SARB has already lifted its repo rate by 500-basis-points since June 2006, by 50 basis points each time. SARB Governor Tito Mboweni said "the central message is that things are going to get difficult before they get better. We all need to act responsibly (when spending)." (Fin24, June 12, 2008)

Current Account Deficit Raises Concern

¶4. (U) Treasury Director-General Lesetja Kganyago, commented that SA
Q4. (U) Treasury Director-General Lesetja Kganyago, commented that SA
is finding it increasingly difficult to finance its current account deficit, which reached 7.5% of gross domestic product in the fourth quarter of 2007. He said global financial market turmoil was contributing to investors opting for other perceived safer-haven markets. SA's low savings rates, coupled with rising investment levels, mean that the country is heavily dependent on foreign savings to finance the large current account imbalance. The SAG-led, multi-billion investment program is likely to keep the current account deficit under pressure over the next few years. This increasing difficulty in financing the current account deficit raises the depreciation risk associated with the rand. This week, the rand lost nearly 1% of its value against the U.S. dollar and

about 0.3% on a trade-weighted basis on concerns of slower global growth and the impact of high oil prices on international inflation. The Treasury is trying to mitigate the currency risk by budgeting for surpluses over the next few years, stating that the SAG is "going to have to save" on behalf of South Africans who "love spending their money". (ABSA Capital Research, June 11, 2008)

Electricity Problems Likely to Harm
Economic Growth Objectives

¶5. (U) SA Deputy President Phumzile Mlambo-Ngcuka said that the SAG's socio-economic development goals may be compromised if the country's electricity problems are not addressed. Although a tighter monetary policy environment contributed to the growth slowdown in the first quarter of 2008, the impact of electricity supply disruptions was clearly noticeable in GDP growth data, especially in the mining sector. The disruption of mining operations (mining contracted by 22% q/q) contributed to overall GDP growth decreasing from an annualized 5.3% q/q in the forth quarter of 2007 to an annualized 2.1% q/q in the first quarter of 2008. Moreover, Minerals and Energy Minister Buyelwa Sonjica expects mines to continue to operate with 90-95% of normal electricity supplies until supply constraints have been addressed. Economists expect the electricity supply constraints to pose a significant risk to the country's medium-term growth prospects. Eskom CEO Jacob Maroga noted that current planning timelines and budgets are going to be missed, which may prolong the electricity crisis. Apart from the electricity supply problems, electricity tariff hikes are likely to worsen the inflation outlook and add upward pressure on interest rates. (Eskom applied for a 60% increase in 2008-09 and NERSA, national energy regulator, is expected to announce a decision on June 18) (ABSA Newsletter, June 10, 2008)

Banks Tighten Discount Screws on Home Buyers

¶6. (U) Integer Home Loan Group CEO Simon Stockley said Absa Bank and First National Bank had changed their credit policies and now required borrowers to deposit at least 5% of the value of the

property to secure a loan. Stockley added that "banks are not going to be as aggressive about offering discounts as they may have been in the past. You are not going to be offered prime minus 2%." Stockley said this had created a "near storm" in a depressed housing market, with first-time home owners affected the most. "Consumers are getting a double raw deal from banks. Not only has the SARB raised interest rate rise by another 50-basis-points on June 12, but banks are reducing the discount on the prime lending rate at which they offer home loans to customers," he said. (Business Day, June 11, 2008)

Cash Is King as Rate Hikes Sting Shoppers

¶7. (U) The credit binge seems to be over, with consumers turning to cash instead of credit. Rising food and fuel prices as well as higher interest rates are putting pressure on disposable incomes, Qhigher interest rates are putting pressure on disposable incomes, making it harder for consumers to service their debt, which will have long-term consequences for credit sales. JD Group Chairman David Sussman said the furniture retailer saw a decline in credit sales of 19% accompanied by a 10% rise in cash sales in the half-year to February 2008 as fuel, food, and interest rates were still climbing. RMB Asset Management Retail Analyst Evan Walker said the debt cycle will have a far-reaching effect on retail sales even when the interest rate cycle turns, as heavily indebted consumers need at least three years of normal economic growth to service bad debts. According to clothing retailer Edcon, which owns Edgars and Jet, credit sales in the year to May slowed, although total sales rose 8.9%. The group, which has more than 4 million active credit card accounts, said credit sales accounted for 53% of total retail sales during 2008, down from 60% in the 2007 financial year. Walker said a shift to cash sales shows "the brakes are really coming on". He said the shift to cash was caused by more people defaulting on in-store credit and fewer people opening credit accounts. The number of account customers who can spend on credit is shrinking, causing the ratio to shift to cash. He expects about 12% of SA's total credit population to come under pressure and default on loans. Consumers are paying off credit, and have learned discipline as a result of the new credit act, which some view as having come too late to protect a burgeoning middle-class.

(Business Day, June 10, 2008)

World Economic Forum on Africa

¶8. (U) Nearly 900 business, government, and civil society leaders from 50 countries participated in this year's World Economic Forum on Africa in Cape Town on June 6. The forum opened with a brainstorming session where education, food security, robust infrastructure, economic growth and investment, and visionary leadership were voted as the top drivers of change. President Mbeki said, "it is necessary to refashion the education system so that when young people come up they are better able to join the economy." Forty leaders from across the continent also launched an Africa Gender Parity Group. (World Economic Forum Press Release, June 6, 2008.)

SA Air Force Pilots Jet-Off to Australia

¶9. (U) The South African Air Force (SAAF) has lost four pilots to Australia this year - a big loss for a service struggling to maintain staff and training levels. The Royal Australian Air Force (RAAF) has also recruited nine other officers with air combat, administrative and logistical expertise. In addition, the SAAF has lost two aircraft technicians, a communications technician, and a clerk from its enlisted ranks to Australia. The RAAF denies charges that it actively recruits personnel under its "lateral" foreigner recruitment program. "A RAAF lateral recruiting team will not be visiting SA," said the Australian Regional Defense Captain Jonathan Mead. It is unclear which country is the main destination for SA Defense Force and Air Force personnel, but the departure of trained personnel is a huge blow. Len le Roux (head of the Institute of Strategic Studies' Pretoria office and a retired Air Force Major-General) said, "there are squadrons where there are 20

aircraft and about four or five pilots." SA's armed forces have long complained about a lack of funding to maintain training levels and retain staff. The Air Force lost more than 240 highly skilled aircraft technicians in 2005. The navy is suffering the same problem. "The Defense Department is indeed concerned with regard to the loss of skilled personnel," Chief Director of Maritime Strategy Bernard Teuteberg said. Air forces always struggle to hold onto pilots in peacetime, Le Roux says. "Government salaries do not compare with those on the outside. He noted that "a guy flying a Boeing to England and back twice a week...gets the same salary as the Chief of the Air Force." The fact that the Australians are recruiting SA pilots shows they are having trouble hanging onto their own pilots, Le Roux added. (Business Day, Weekender, June 7-8, 2008)

Delta Optimistic About Africa Expansion

¶10. (U) Delta Airlines Sales Manager for Southern Africa Margaret Copeland is optimistic about Delta's expansion strategy in Africa. Delta started direct service from JFK to Cairo and from JFK (via Dakar) to Cape Town on June 3. The new service to Cape Town will leave Cape Town four days a week on Mondays, Wednesdays, Fridays, Qleave Cape Town four days a week on Mondays, Wednesdays, Fridays, and Saturdays. Delta plans on adding a second daily flight to Lagos and starting service to Nairobi (also via Dakar) in June 2009, after having been postponed a year as a result of the recent violence in Kenya. The airline is creating a mini-hub in Dakar for its Africa service. Copeland noted that sales for the Cape Town route were brisk (about 65%, with even higher occupancy in business class) and expected sales to pick-up once the winter season ended. The service from Cape Town will also carry cargo, including flowers, fish, trophy animals and perhaps fresh fruit to the U.S. In the long-term, Delta would like to increase the frequency of the service to Cape Town to daily service and switch to from the current Boeing 767-300ER to a larger Boeing 767-400ER if passenger traffic increases. The Boeing 767-300ER accommodates 217 passengers (36 business class and 181 economy class seats). Delta is also interested in expanding service from the U.S. to Morocco and Angola to strengthen its presence in Africa.

Airports on Track for 2010, But ACSA   Concerned about High Borrowing Costs
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¶11. (U) Airports Company of SA (ACSA) CEO Monhla Hlahla announced

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that SA's three major airports - OR Tambo International, Cape Town and Durban International - would be ready by 2010 for the thousands of FIFA World Cup visitors. She noted that ACSA had modified its existing expansion plans when the games were announced to accommodate the peak traffic arriving in 2010 during the weeks of the World Cup. Hlahla said about 350,000 more passengers would be arriving in SA during the event. The company will spend R22 billion ($2.8 billion) towards the building and renovation of the country's airport infrastructure. The smaller airports in Bloemfontein, Port Elizabeth and East London are also being refurbished. However, ACSA officials noted that it may have to postpone some of its projects because of the current high cost of borrowing. The company plans to raise about R10 billion ($1.3 billion) to meet its financial need for airport construction and up-grades. Hlahla said, "It has been very difficult. We issued a bond program and we tried to borrow against the program, but the prices were just too high. If the cost of capital continues the way it has, we may have to reconsider some of our development and postpone them to a later stage." ACSA is also faced with serious security challenges at its major airports. It will spend R46 million ($5.8 million) on security at OR Tambo International Airport ahead of the World Cup. (Business Day and SABC News, June 11, 2008)

Guatrain on Track for 2010

¶12. (U) Nearly 5 km of the 15 km underground route of the R25 billion ($3.2 billion) Gautrain project has been completed. The 80 km project will connect Johannesburg, Pretoria, and OR Tambo International Airport by 2011. The airport link to Johannesburg is expected to be completed in time for the 2010 FIFA World Cup. The Gautrain system will include park-and-ride facilities and 150 buses to provide local transport in a ten-kilometer radius around each station. Gautrain's 24 trains will be maintained and serviced at a new train depot. A bus depot will also house the Gautrain's dedicated fleet of 150 luxury buses. Construction of these facilities is well advanced, with the bus depot administration building already complete and the train depot offices and maintenance workshops targeted for completion within the next few months. (Engineering News, June 6, 2008)

Motor Industry Running on Empty

¶13. (U) Four years of booming motor industry sales accompanied by huge investments have come to a halt as the industry faces dealership closures and job losses. May vehicle sales (12,095 units) represented the largest decline in nine years. Sales in three of the four market segments have decreased in 2008. Passenger vehicle sales declined by 19%, light commercial vehicle sales were down 9%, and medium commercial sales dropped by 0.4%. The only market segment to experience growth was the heavy commercial vehicle segment, which increased 15.6%. Analysts noted that the possibility of further interest rate hikes was undermining vehicle sales. (Business Day, June 2, 2008)

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Mercedes-Benz SA Expands Truck Range

¶14. (U) Mercedes-Benz SA (MBSA's) has expanded its Axor truck range to include an extra-heavy-duty 6x4 truck tractor and freight carrier. The Axor range was first introduced to SA at the end of 2003, and has since recorded sales of more than 1,650 units in the extra-heavy segment of the truck market. MBSA Commercial Vehicle Product Manager Peter Wraight stated that the new addition follows "extensive market research". The new Axor 6x4 is available in 350 and 400 horsepower models. It is the "culmination of ten years of planning and collaboration between Mercedes-Benz Germany, and the local engineers at the truck research center in East London and development centers in Turkey and Brazil," he said. MBSA Commercial Vehicle Manager Kobus van Zyl said the new Axor enters the "most competitive market for Mercedes-Benz worldwide", with more than 30 trucking companies vying for customers' attention. He added that the booming SA truck market is expected to reach sales of more than 40,000 units in 2008 and continue to grow. The local truck market

broke through the 37,000 unit barrier in 2007, recording its best sales performance ever - this while passenger vehicle sales limped into negative territory. Van Zyl said the SA truck market could reach 51,000 units by 2012, a level he believes is "definitely sustainable". MBSA, the current market leader, is expected to increase its share of the truck market from last year's 3,287 units, to more than 4,400 units in 2008. The truck market is being driven by factors such as SAG's infrastructure spending and increasing demands on the freight market, which has been able to outpace the current global economic turmoil. The first orders for the new Axor range has come from coal haulers. Eskom indicated earlier this year that the power crunch has increased its coal requirements substantially, which has had a positive impact on the local coal-mining and coal-hauling markets (and a negative impact on the road system. (Engineering News, June 6, 2008)

Electricity Distribution Maintenance Backlog - Another Electricity Crisis Looms
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¶15. (U) Electricity authorities called for action to deal with a large maintenance backlog that could further stifle economic growth. SA Local Government Association Chairman Amos Masondo told the Electricity Distribution Maintenance Summit on June 9, "the current electrical infrastructure maintenance and refurbishment backlog is estimated at R26.7 billion ($3.5 billion), on the basis of a recent analysis." Speakers warned that underinvestment in ageing infrastructure could plunge SA into another electricity crisis. Minerals and Energy Minister Buyelwa Sonjica told delegates that the government had invested about $200 million annually into new electricity distribution infrastructure, but admitted little money had been injected into maintenance. She said, "the lack of maintenance and refurbishment of the electricity distribution infrastructure poses a threat to our economy." She continued, "The upcoming 2010 FIFA World Cup and the rapid economic growth of the country demand more improvement on the capacity of the electricity distribution infrastructure." The Ssummit also discussed the stalled implementation of regional electricity distributors (REDS), which will take over power distribution from municipalities. Deputy President Phumzile Mlambo-Nguka told delegates there was resistance to implementing this new system, but insisted there are mechanisms to ensure that municipalities and Eskom would not lose out. Eskom is embarking on a $50 billion electricity generation capital expansion program. (Engineering News and Business Day, June 10, 2008)

Minister Says Suez Energy Submitted Binding Offer for IPP Project
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¶16. (U) Minerals and Energy Minister Buyelwa Sonjica said in her recent budget speech to Parliament that Suez Energy of France, which was short-listed with U.S. firm AES, had shown a "strong commitment" to becoming a developer of the Department of Minerals and Energy's (DME) independent power producer (IPP) "peaking" project. AES Q(DME) independent power producer (IPP) "peaking" project. AES recently withdrew its offer for the project. DME announced the receipt of a binding offer from a Suez-led consortium for the construction of two open-cycle gas turbines totaling 1,000 MW. Minister Sonjica qualified this as "an irreversible process of establishing IPPs on the journey to achieving our target of 30% private power generation". Sonjica again urged electricity users to conserve more power, noting that the SAG was finalizing a regulatory framework to ensure that the DME's Power Conservation Program was enforced with penalties for excessive use and wastage of electricity. (Engineering News, June 6, 2008)

U.S. Gold Miner in SA

¶17. (U) U.S.-based Eastern Goldfields recently bought Barbrook Gold Mine in Mpumalanga for $10 million and plans to raise $30 million in cash through a listing on the Johannesburg Stock Exchange. The company said the funds would be used to complete development of the Lily underground gold mine and a nearby metallurgical plant, also in Mpumalanga. (Business Day, June 10, 2008)

Canadian Business Chamber Flays SA

¶18. (U) Canada-SA Chamber of Business President Bruce Shapiro asserted at the June 9 African Mining Congress that SA's energy crisis was of its own making and showed that leadership was incompetent. Shapiro heads the Toronto-based, independent business chamber which is focused on the resource sector. He cited a number of other challenges in SA:

* Looming change in political leadership is a risk.
* Crime is the "Achilles heel" in SA.
* SA has not addressed sustainable water supply.
* Skilled labor shortages and obtaining work permits are problems.
* Beneficiation policies are wrong.
* Little has been done on HIV/AIDS.
* Processing of mineral licenses is slow.
* Lack of transparency and political uncertainty are issues.

Unions Give Telkom Silent Treatment

¶19. (U) Trade unions representing 70% of Telkom staff announced that they would not engage in any further negotiations until the fixed-line operator agreed to undertake a thorough investigation into its outsourcing restructuring plans and signed a "no job loss" agreement with them. The Communication Workers' Union (CWU), Solidarity, and the SA Communications Union said they would oppose the restructuring if it would lead to job losses. The unions are conducting a study to determine the effects of the restructuring. The findings will be submitted to the Independent Communication Authority of SA (ICASA). "If Telkom's plans are approved, more than 90% of jobs in the company will be affected," they said. The unions said Telkom's deadline for final approval for the restructuring, which it wanted to achieve by August, would not be reached. (Business Report, June 11, 2008)

Dubai World Plans to Expand in SA

¶20. (U) Dubai World Chairman Sultan Ahmed Bin Sulayem told the World Economic Forum on Africa that the keys to unlocking the potential of Africa were investment in infrastructure and education. He noted that, "with solid infrastructure and excellent human resources, other developments such as real estate, retail properties and tourism can be established, contributing further to the economy." Dubai World, which is the investment arm of the Dubai government, acquired a major shareholding in three SA wildlife reserves for an undisclosed amount in March 2008. The company acquired Shamwari Game Reserve in Eastern Cape, Sanbona Wildlife Reserve in Western Cape and Jock Safari Lodge in the Kruger National Park. Sulayem was reluctant to disclose the amounts his company would spend in SA, but said the money would come from the $1 billion fund earmarked for projects in Africa over the next five years, in addition to the $4 billion already committed. He said Dubai World would build more luxury lodges in the wildlife reserves as well as a five-star hotel and 60 private apartments at Pearl Valley Golf Estate in the Cape vine lands. Dubai World is also expanding the Victoria & Alfred (V&A) Waterfront in Cape Town to double the space available for prospective hotel, leisure, and retail tenants. "Our projects for Qprospective hotel, leisure, and retail tenants. "Our projects for the V&A Waterfront expansion (as well as the) Pearl Valley hotel and apartments and Shamwari lodges are in the planning stages," Sulayem said. The company is formulating plans to make the Nkomazi game reserve in the Mpumalaga Province eligible to become a World Heritage site. The company will open a 24-bed luxury tented camp at the game reserve in November. The development would also include seven secluded five-star boutique hotels and lodges with a total of 120 beds, a 36-hole championship golf course, a residential estate, 25 luxury private residences and 425 "eco-residences". Projects outside SA include a $70 million five-star hotel in the Comoros, and a $250 million hotel in Djibouti. (Business Day and Dubai World Press Release, June 6, 2008)

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